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Nos. 143, 159 and 576

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In the Supreme Court of the United States

OCTOBER TERM, 1965

THE BALTIMORE AND OHIO R. Co., *et al.*, *Appellants*, vs. THE ATCHISON, TOPEKA AND SANTA FE RY. Co., *et al.*, *Appellees.*	No. 143
CHICAGO AND NORTH WESTERN RY. Co., *et al.*, *Appellants*, vs. THE ATCHISON, TOPEKA AND SANTA FE RY. Co., *et al.*, *Appellees.*	No. 159
UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION, *Appellants*, vs. THE ATCHISON, TOPEKA AND SANTA FE RY. Co., *et al.*, *Appellees.*	No. 576

On Appeal from the United States District Court for the Southern District of California, Central Division

Motion to Affirm

MARY MORAN PAJALICH
RODERICK B. CASSIDY
J. THOMASON PHELPS
CYRIL M. SAROYAN
State Building
San Francisco, California 94102
Attorneys for Intervening Plaintiffs-Appellees, the People of the State of California and the Public Utilities Commission of the State of California

BORG PRINTING COMPANY OF CALIFORNIA, 346 FIRST STREET, SAN FRANCISCO 94105

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Intervening plaintiffs-appellees, the People of the State of California and the Public Utilities Commission of the State of California, pursuant to Rule 16 of the Revised

Rules of the Supreme Court of the United States, move that the judgment of the District Court be affirmed on the ground that the questions are so unsubstantial as not to warrant further argument.

STATEMENT

This case is a direct consequence of the extraordinary population, industrial and agricultural growth of the West, and particularly of the State of California, during the past four decades. This Western development has in part been responsible for similarly profound economic changes in other parts of the nation, particularly in the Northeast, where the long established industrial monopoly has been broken and companies encouraged to move westward. American railroads have been profoundly affected by this modern industrial revolution, primarily because of the enormous investment in facilities and equipment necessary to provide rail service. In the West, although railroads found their gross revenues increasing, they found the need for new investment in facilities and equipment to meet the needs of the expanding West increasing while their net operating income remained static. By contrast, Eastern and Midwestern railroads were faced with a substantial loss of revenue and over-capacity as a result of the loss of population and industry to the West combined with the lessening of the Northeastern control over nationwide markets. This divisions case represents an effort by the Eastern and Midwestern railroads to off-set the losses incurred as a result of the industrial shift to the West by obtaining increased percentages of transcontinental freight rates.

A primary issue before the Interstate Commerce Commission was the relative situations of the Eastern, Midwestern and Mountain-Pacific railroads with respect to "the

amount of revenue required to pay the railroads' respective operating expenses, taxes, and a fair return on their railway property held for and used in the service of transportation," which is one of the factors which Section 15(6) of the Interstate Commerce Act requires the Commission to consider. Each group of railroads before the Commission contended that this revenue needs factor weighed heavily in its favor. The Eastern and Midwestern railroads claimed greater revenue needs on the theory that the loss of population and industry to the West had left them with lower rates of return than the Mountain-Pacific railroads; the Mountain-Pacific railroads claimed greater revenue needs because the extraordinary growth of the West had imposed such enormous investment responsibilities upon them that despite their somewhat higher rates of return, they had less money available for distribution to their stockholders than either of the other groups of railroads. As representatives of the public interest, the People of the State of California and the California Public Utilities Commission supported the position of the Mountain-Pacific railroads that the proper measure of revenue needs was the actual needs of the railroads to meet their public responsibilities, not merely the nominal rates of return which they happened to realize. Accordingly, we asked the Commission to determine the basic revenue needs issue in light of the different investment responsibilities faced by the railroads in the various parts of the country by calculating the revenue needs of each group of railroads in terms which took this difference into account.

In its reports, the Commission agreed that relative revenue needs was the primary factor to be taken into account in making divisions of the revenues involved in this case (B&O J.S. 95a), but it then proceeded to order increases

in the divisional shares of the Eastern and Midwestern railroads, without finding either what the revenue needs of the various groups of railroads actually were, or the effect its new divisional order would have upon the Mountain-Pacific railroads which were to bear the brunt of the increases ordered for both the East and the Midwest. The United States District Court for the Southern District of California set aside these orders of the Commission, and these appeals followed.

ARGUMENT

The district court set aside the Commission's orders on the ground, among others, that the Commission's treatment of the issue of relative revenue needs failed to comply with applicable statutory standards. And these appeals, which because of intervening settlement agreements, are being actively pressed only by certain Midwestern railroads and by the Commission on their behalf, challenge the district court's determination principally as it relates to that ground. But it is manifest that the questions presented by appellants with respect to the issue of relative revenue needs are so unsubstantial as not to need further argument.

I. The District Court Properly Set Aside the Commission's Orders for Failure to Resolve the Basic Revenue Needs Issue in the Case.

The district court rejected appellants' contention that by findings stated wholly in terms of rates of return and freight income excluding passenger deficits, the Commission had fully discharged its duty under Section 15(6) to give due consideration to the relative revenue needs of the carriers involved (B&O J.S. 19a-20a). This holding was plainly correct, and, indeed, in view of the issues raised by the parties in the proceedings before the Commission,

absolutely necessary under the explict requirements imposed upon the Commission by Section 8(b) of the Administrative Procedure Act to make findings sufficient to resolve all the material issues presented to it.

As stated above, the basic revenue needs issues before the Commission grew out of the vastly different economic situations in which the various groups of railroads involved here found themselves. The Eastern railroads and, to a somewhat lesser extent, the Midwestern railroads, are overbuilt in terms of the present economies of the regions which they serve. The Mountain-Pacific railroads, on the other hand, serve a region which faces a critical need for additional transportation facilities.* The basic revenue needs issues before the Commission related to the problem of deciding just what the actual needs of the railroads involved were. Were there substantial differences in the investment responsibilities of the various groups of railroads? To what extent were the Eastern and Midwestern railroads' operations affected by overcapacity? To what extent did the Mountain-Pacific railroads face a need for making expenditures without any prospect of recovering such expenditures through increased revenues in order to bring the level of rail service in the West up to that already enjoyed in the East?

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*This difference is shown by uncontroverted evidence in the record, having been expressly admitted by the Eastern and Midwestern railroads themselves. The president of the New York Central Railroad testified, for example:

> "You have to contract facilities today in the East rather than expand them." (Tr. 1486).

The Pennsylvania railroad witness agreed that Eastern roads have "shrinking plants" (Tr. 381-382, 9830). The contraction of railroad plant in the East and Midwest is exemplified by Pennsylvania's program to eliminate thousands of miles of track (Ex. T-336, p. 37; Tr. 9830-31), the New York Central's program for eliminating mileage of "unnecessary tracks" (Ex. T-106, p. 20) and the Chicago & North Western Railway's program for abandonment of line and other elimination of excess track (Ex. T. 350, pp. 17-19; Ex. MW-453).

The Commission failed utterly in its duty to resolve these issues. Although the revenue needs issues presented by the parties could only be resolved by consideration and evaluation of the actual needs of the various groups of railroads in the particular differing economic situations in which they operated, the Commission made no findings at all related to such matters. Instead, it merely reviewed the rates of return of the various groups of railroads and compared their theoretical earnings as freight carriers, by excluding their respective passenger deficits,* without even trying to determine by any rational standard just what the revenue needs of the various groups of railroads actually would be. The Commission simply shrugged off this part of its responsibility (B&O J.S. 96a):

> "We are unable to agree with the defendants and the interveners that the public interest warrants increases in the divisions of the mountain-Pacific railroads in order to provide a source of investment funds required for enlarged facilities commensurate with industrial development in that region. The railroads in all sections of the country are faced with the continuing necessity of raising funds for additions and betterments and new equipment, and we cannot recognize any difference in the degree of this urgency among the territorial groups."

Before the district court, these interveners pointed out that this cryptic pronouncement did not satisfy the requirements of Section 8(b) of the Administrative Procedure Act. The uncontroverted evidence before the Commission showed a wide difference between the investment needs of the railroads serving California and those serving the Eastern

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*As pointed out below (p. 13), this passenger deficit theory represented an independent error of the Commission, which the district court quite properly condemned, and upon which the district court's judgment could, if necessary, be independently sustained.

areas where industry was declining and the railroad system was already overbuilt, and the Commission did not deny this.* Why then did the Commission refuse to recognize this difference in determining the revenue needs of the carriers? The Commission's reports simply do not disclose the answer to this critical question. Accordingly, interveners presented the following issue to the district court, which was included as Issue No. 19 in the stipulated List of Issues Remaining in Controversy prepared by the parties at the direction of the district court.

> 19. Whether plaintiffs' and intervening plaintiffs' claim that differences in requirements for investment funds for equipment and facilities commensurate with industrial development in the territories served by the respective carriers should be considered in determining revenue needs was a material issue within the meaning of Section 8(b) of the Adminsitrative Procedure Act; and, if so, whether the Commission stated findings and conclusions, as well as the reasons or basis therefor, upon such issue?

The district court resolved this issue by holding that the issue was material and, therefore, that "findings must be made as to the amount of revenue, *in terms of dollars,* required by the respective carriers affected in any new divisions prescribed . . ." (B&O J.S. 20a) (emphasis supplied). Appellants criticize this holding that revenue needs findings must be made in terms of dollars (C&NW J.S. 16-20; J.S. 15-18), but no effort is made to suggest any other standard for measuring revenue needs which would have resolved the basic revenue needs issues before the Commission. Certainly, the contention that rates of return are in themselves adequate—which contention is the only one appellants

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*Indeed, elsewhere in its report, the Commission affirmatively and explicitly recognized the different economic and transportation conditions in the various parts of the country (B&O J.S. 72a-73a).

have made, either before the district court or in their jurisdictional statement here—is demonstrably unsound. The whole revenue needs issue presented to the Commission was to what extent rates of return had to be adjusted to measure actual revenue needs. A recital of group average rates of return certainly does not resolve that issue.

The district court was thus eminently correct in holding that the Commission had to go further in order to fulfill its duty in this case. Section 8(b) of the Administrative Procedure Act unequivocally requires that the Commission make findings on all material issues before it. Since the revenue needs issue was not only material but critical under the view the Commission chose to use as the basis of its decision here, it was imperative that its findings on that issue be stated in terms which would rationally resolve the controversy between the parties. We do not suggest that the Commission was under a statutory obligation to decide the merits of the revenue needs issue in the precise way we contended for. But it was under an obligation to decide the question, and it could not lawfully simply shrug it off.

Appellants' attempt to have the Court disregard the absence of findings by the Commission, and, in effect, substitute its own findings by approving a report which does not resolve the basic issues before the Commission should therefore be rejected.

II. The District Court's Decision in No Way Interferes with the Administration of Section 15(6).

Appellants' second main ground of attack upon the holding below is their claim that the district court has made Section 15(6) of the Interstate Commerce Act unworkable for any practical purpose by requiring the Commission to make findings which show that the standards of Section 15(6) have been observed with respect to each of hundreds of carriers involved in this case (C&NW J.S. 11-16; U.S. J.S. 10-13). There is no substance whatever to this claim.

The district court's holding rests principally upon the ground that the Commission's findings were inadequate with respect to the carrier *groups*. This was the principal issue before the district court. Indeed, this was the only issue presented by these interveners, for, as representatives of the public, our concern was not with any particular railroad but with the ability of the whole group of railroads which serve California to meet the transportation needs of the people of our State. Our position, both before the Commission and before the district court, was that although the Commission unquestionably had the ultimate power under Section 15(6) to decide this controversy in the national interest, it was also bound by that Section to give due consideration to the interests of people of the West and to dispose of their arguments only on the basis of rational findings. This the Commission plainly failed to do.

As the district court held (B&O J.S. 12a), it is axiomatic that, whatever the basis of an order prescribing divisions may be, the effect of that order must be known and found as a prerequisite to its validity. This is so, in the first place, because, unless the Commission considers and determines on an individual basis the proper division of each joint rate at issue—a wholly impractical possibility never attempted by the Commission—the soundness of its ultimate order will inevitably depend in substantial part upon the overall effect of that order. Whether the Commission chooses to base its decision upon relative costs alone, or relative revenue needs, some other factors permitted by Section 15(6), or any combination of these factors, the Commission cannot measure its order against the factor or factors chosen without

knowing just what its order does. The Commission must know and find what any contemplated order would do to the revenues of the railroads involved before it can begin to perform its plain statutory duty.

In a case such as this one, where the Commission actually relied upon relative revenue needs to support its orders, the need for such findings is even clearer. A change in divisions on asserted grounds of revenue needs, without knowledge of the amount being transferred to the Eastern and Midwestern railroads, does not tell us whether the alleged revenue needs of those roads are being met. It cannot be ascertained whether the increased divisions would or would not be in excess of the contributions which transcontinental freight traffic ought to make to the Eastern and Midwestern roads.

The Commission violated this principle here. It nowhere found, and, indeed, denied that it has any responsibility to find, the actual financial impact of those orders. Nor did the Commission find what the impact of the orders should be. Thus, the Commission's decision was that the Eastern and Midwestern railroads should have an indeterminate increase in their divisions to reflect relative costs and relative revenue needs. And the Commission's orders prescribed an increase in those divisions—also indeterminate both in amount and in relationship to the basic decision of the commission. This process was plainly irrational and unlawful.

How would this transfer affect the revenue needs of the Western railroads? Would it impair the financial ability of these lines in performing their service obligations and meeting the needs of the public in their own territory? The revenue effect of the Commission's order must be determined so as to make the above determinations.

The Commission asserted at page 76 of its Original Report (dated March 21, 1963) that "Under the requirement of

the public interest that all essential parts of the transportation system be maintained, so far as possible, in effective working condition, we believe that there should be increases in the complainant's divisions reflecting revenue need . . ." This was an ultimate finding, and, as such, it is sound only if, "Every issue that must be resolved to reach that ultimate finding" has itself been resolved by findings. *California Motor Transport Co. v. Public Utilities Commission,* 59 Cal. (2d) 270, 273, 379 P.(2d) 324, 326 (1963).

In this case, the Commission's ultimate finding on the revenue needs issue was wholly without support in essential underlying findings of fact. There was no finding identifying the particular transportation needs which it is necessary to protect by transfer of divisional revenues. There was no finding of the amount of revenue necessary to accomplish the objective required by the public interest. The resulting substantial change in revenues of the Mountain-Pacific lines would inevitably have a substantial effect upon the ability of those lines to meet the transportation needs of the public. Would this change help or hurt the overall public interest? This is not ascertainable.

Bearing in mind, always, that as to the Eastern railroads as a whole, transcontinental freight traffic makes up but 6 percent of the total freight traffic, any increase in divisions, in whatever amount, could have little effect on the overall financial condition of those roads and their ability to serve the public. As for the Midwestern lines, only 15 percent of their total freight revenues is received from transcontinental freight traffic. Hence, the increase in divisional revenues to those two groups of roads would be borne by a few principal Mountain Pacific roads who depend for half of their total freight revenues on these divisions. The ability of these Western railroads to serve the rapidly growing areas in the West would be impaired completly out of proportion to the benefit to the total operations of roads in the East and

Midwest. Transcontinental freight traffic is only of minor importance to the financial condition of those roads. The significance of the relative importance of transcontinental freight traffic to the respective groups is that a transfer of divisional revenues from the Western railroads to the Eastern and Midwestern railroads would severely impair their ability to serve the public of the expanding West without producing any real improvement in the financial position of the Eastern and Midwestern lines.

The Commission's reports identified neither the parts of the transportation system which must be maintained in effective working condition through a transfer of divisional revenues nor the amount of revenues required to reach that objective. It is true that the reports stated that there are differences in earning power and that the Eastern railroads are in a less advantageous situation as freight carriers. But these statements rest upon an erroneous passenger deficit theory which none of the appellants even attempts to defend in this Court. In addition, these statements were highly generalized and made no effort actually to identify and evaluate the needs of the Eastern and Midwestern railroads even under the Commission's erroneous theories.

The parties, in the district court and now in this Court, are thus left to guess as to the effect of the Commission's orders and the relationship between those orders and the Commission's basic decision that the transcontinental divisions should reflect the broader aspects of revenue need. The People of the State of California think it plain that something more is required of the Commission in a case involving the public interest to the extent this case does. In any case where the issue before the Commission is the amount of revenue which a carrier should get from one part of its business in order to insure a just contribution to its

overall revenue needs, an absolute prerequisite to rational, lawful decision is a determination as to the amount of the overall needs and the amount of the transfer that should be made to meet those needs. Since the Commission is compelled by law to decide the controversies before it only in a rational and lawful way, such a determination should have been made here.

Treated on the basis of carrier groups alone, as appellants insist, the Commission's order is therefore plainly unlawful. The district court also found that three individual railroads had not waived their rights to individual consideration of the special impact of the Commission's order upon their special situations (B. & O. J.S. 19a). This holding, supported by a careful review of the authorities (B. & O. J.S. 19a), hardly warrants the assertions of appellants that compliance with the Administrative Procedure Act will impair the Commission's administration of divisions cases (*e.g.*, U.S. J.S. 18). But whatever the rights of these individual railroads might be, they surely do not detract from the rights of the People of the State of California to a lawful determination of their interest in maintaining the whole transportation system necesssary to the economy of this State.

III. The District Court Also Properly Held That the Commission's Exclusion of Revenue Needs Reflected in Passenger Deficits Was Unlawful.

The district court was also clearly correct in holding that the Commission must consider "the revenue needs of the carriers from *all* transportation services, including needs represented by passenger deficits" (B. & O. J.S. 20a). Other parties will argue more fully the correctness of the district court's decision on this separate point. It suffices for these appellees to state that the Commission has relied upon the revenue needs of the railroads serving California from all

of their operations, including passenger operations, in requiring increases in California intrastate freight rates. *California Intrastate Rates and Charges,* 302 I.C.C. 189, 192-196 (1957), applying the approach approved by this Court in *King v. United States,* 344 U.S. 254 (1954). Certainly in the absence of findings reconciling such action, the Commission cannot lawfully administer the same statute concerning the same revenue needs of the same railroads by determining revenue needs on one basis in increasing freight rates, and then reducing the divisions of the same railroads on a different and inconsistent basis.

CONCLUSION

For the foregoing reasons, the Judgment of the district court is clearly correct and no substantial questions for the decision of this Court are presented by these appeals. The Judgment of the district court should be affirmed without argument.

Respectfully submitted,

Mary Moran Pajalich

Frederick B. Haserey

J. Thomason Phelps

Cyril M. Sarafian

Attorneys for Intervening Plaintiffs-Appellees, the People of the State of California and the Public Utilities Commission of the State of California

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